

STATE OF IOWA
DEPARTMENT OF COMMERCE
UTILITIES BOARD

IN RE: QWEST COMMUNICATIONS INTERNATIONAL INC. SALE OF PUBLISHING BUSINESS	DOCKET NO. WRU-02-37-272 (SPU-02-15)
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ORDER REGARDING REQUEST FOR WAIVER

(Issued October 3, 2002)

PROCEDURAL HISTORY

On August 20, 2002, Qwest Communications International Inc. (QCII) announced an agreement to sell its QwestDex directory publishing business to a nonaffiliated entity. QCII's press release regarding the sale implies a belief on the part of QCII that regulatory approval of the proposed transaction is not required in Iowa. However, based on the limited information available to the Utilities Board (Board) at the time of the press release, it appeared to the Board that regulatory review may be required in Iowa before the transaction may be closed.

In order to determine the scope of its jurisdiction regarding this matter, the Board issued an order in this docket on August 21, 2002, directing that on or before August 28, 2002, Qwest Corporation (Qwest) file an application for approval of the proposed reorganization, a request for a waiver of the review requirement, or a detailed explanation of the basis for Qwest's apparent belief that review is not required in Iowa. Other interested parties, including the Consumer Advocate Division

of the Department of Justice (Consumer Advocate), were invited to file comments at the same time regarding the application of Iowa Code §§ 476.76-.77 (2001) to these circumstances. Timely filings were made by Consumer Advocate, the Carlyle Group and Welsh, Carson, Anderson & Stowe (collectively, the Buyers), and Qwest, the public utility subsidiary of QCI that offers regulated local exchange service in Iowa.

On September 4, 2002, the Board issued an order finding that it has jurisdiction to review the proposed transaction pursuant to Iowa Code § 476.77 and that, in the absence of a waiver issued pursuant to § 476.77(4), the transaction cannot take place until the Board's review is completed. The Board found that to the extent the sale of QwestDex could make imputation impossible in the future, the sale is an indirect disposition of the public utility asset of imputed revenues.

However, the Board also stated that as a possible alternative to a complete review proceeding, Qwest could request a waiver of that review pursuant to § 476.77(4), which authorizes the Board to grant a waiver where review is not necessary in the public interest. In balancing the public interest in granting a waiver, the Board recognized the following points that would tend to weigh in favor of waiver:

1. A binding assurance from Qwest that in any future rate proceeding of any nature, it will be precluded from arguing against imputation on the grounds that the directory publishing business has been sold. Qwest could reserve any other arguments it may have against imputation, as well as the opportunity to suggest appropriate methods for calculating imputed revenues in a future rate proceeding.

2. Specific assurance from Qwest that sufficient capital will continue to be invested in Iowa to maintain service quality that meets or exceeds all requirements in Board rules and the Qwest/U S West settlement.
3. Specific assurance from Qwest that bidding in any future sale of Iowa rural exchanges will be structured to allow bids for only Iowa exchanges.
4. Information to support a Board finding that Board review of the QwestDex sale is not necessary in the public interest because of the effect on the financial stability of Qwest caused by the delay inherent in review.

Based on its finding of jurisdiction, the Board directed Qwest to file a proposal for reorganization regarding the proposed sale of QwestDex or a request for a waiver of that review before the proposed sale is closed to allow for Board review of the proposal or request.

REQUEST FOR WAIVER

On September 19, 2002, Qwest filed a request for an expedited waiver of the reorganization statutes and rules, to the extent they apply. Qwest states that the public interest does not require full reorganization review of the proposed transaction and a waiver is therefore appropriate.

First, Qwest argues that the proposed transaction will not adversely impact day-to-day telecommunications services or rates in Iowa and will not result in any material changes in telephone directories. Qwest argues the change in ownership of

the directory operations will be transparent to consumer from the perspective of the directory.

Qwest also addressed the four specific factors identified in the Board's September 4, 2002, order. First, Qwest committed that

for the term of the current price plan in Iowa, and for an additional term if that price plan is renewed without substantial changes, Qwest will not initiate a proceeding to change rates on the theory that imputation must end because of the sale of its directory publishing business to Buyer in this transaction. Qwest would, however, remain free to make any other arguments relating to imputation, and to address appropriate methods for calculating any imputed revenues in any future proceeding. Further, Qwest reserves the right to argue that imputation should end because the directory publishing business has been sold in response to any filing made by any other party relating to rates or exogenous changes under the price plan.

(Request for waiver, page 6.)

Second, Qwest committed that it "will continue to invest capital in Iowa sufficient to meet or exceed all applicable requirements in Board rules as well as the merger docket Order, in accordance with the provisions contained therein." (Request for waiver, page 7.)

Third, Qwest stated that it does not contemplate any sale of exchanges at this time, but "in the event that Qwest decides in the future to sell exchanges in Iowa, Qwest will consider bids from all interested parties, including Iowa parties, and will structure the sale process to ensure that bidders are able to submit bids for Iowa properties only." (Id.)

Finally, Qwest stated that the proposed transaction is a critical part of its overall strategy to "de-lever" the QCII balance sheet and ensure the financial stability of QCII and Qwest. The sale of the directory publishing assets in a timely manner is integrally related to Qwest's recently completed refinancing efforts, and a protracted review process could compromise the transaction, which must close by December 15, 2002, or either party may terminate the agreement. Qwest expressed the desire to close the transaction much earlier than that date, in order to reduce market uncertainty on both sides.

On September 20, 2002, Qwest filed the non-confidential parts of the transaction documents, and on September 24, 2002, Qwest filed the confidential parts of the transaction documents, along with a request for confidential treatment of those documents.

CONSUMER ADVOCATE'S OPPOSITION TO WAIVER

On September 19, 2002, the Board issued an order requiring that any responses to Qwest's request for an expedited waiver be filed no later than September 27, 2002. Pursuant to that order, Consumer Advocate filed a timely opposition to Qwest's waiver request. Consumer Advocate argues that waiver is the exception, not the rule, and that Qwest has not demonstrated that Board review of the proposed transaction is not necessary in the public interest.

Consumer Advocate argues that Qwest's first commitment, a qualified assurance that Qwest will not argue against imputation in a future rate proceeding on

the grounds that the directory publishing business has been sold, is inadequate. The commitment "has a series of loopholes under which Qwest will **not** be precluded from arguing against imputation on the grounds that the directory publishing business has been sold, *i.e.*, (i) if the price plan is not renewed; (ii) if the price plan is renewed with changes; or (iii) if any party other than Qwest makes any filing relating to rates or exogenous changes under the price plan." (Opposition at page 2, emphasis in original.) Consumer Advocate argues this commitment is "hollow and empty." (Opposition at page 3.)

Consumer Advocate also argues that Qwest's second and third commitments are "exceedingly short and essentially unenforceable" (Id.) Consumer Advocate argues the purported commitments fall short of the Board's "requirement," but does not explain how they fall short.

Finally, Consumer Advocate says Qwest's attempt to show that Board review of the QwestDex sale is not necessary in the public interest is unsupported. Consumer Advocate concludes that Qwest has failed to accept the Board's September 4, 2002, suggestions regarding the showing Qwest must make and, as a result, the waiver request should be denied.

ANALYSIS

The Board will deny Qwest's request for waiver because it falls short of demonstrating that review of the proposed transaction is not necessary in the public interest. In particular, the Board is concerned that the duration of the commitment

Qwest has offered with regard to its arguments in any future rate review proceedings is inadequate and the limitations on the commitment are unreasonable.

1. The commitment concerning future rate case arguments

The commitment offered by Qwest with respect to future rate case arguments is limited to the remaining term of Qwest's existing price regulation plan, plus three more years if the plan is renewed without substantive changes. This means that Qwest could come before the Board at the end of the existing price regulation plan in November of 2004 and argue that imputation must end because of the sale of its publishing affiliate. The Board has already stated that a commitment of only two years' duration, representing the remaining term of the existing plan, "is not sufficient to satisfy the Board that review of the proposed transaction is not necessary in the public interest." ("Order Finding Jurisdiction," page 8, issued September 4, 2002.)

Qwest does not offer any explanation for its apparent belief that a commitment regarding Qwest's use of an argument against imputation based on the sale that is as short as two years is an adequate substitute for the permanent commitment identified in the September 4, 2002, order. The point of this commitment is to eliminate one of the public interest factors that would otherwise have to be considered by the Board in a full-blown reorganization review proceeding, that is, the effect of the sale of these assets on the continued viability of imputing directory publishing revenues. That factor is fully addressed only by a commitment that is not subject to any specific time limitations.

This does not mean the commitment must be permanent. The Board understands that the telecommunications industry is constantly changing and that the circumstances supporting imputation may change in the future. The Board would accept a commitment as described in the September 4, 2002, order, but reserving to Qwest the right to argue, in a future proceeding, that material changes in circumstances mean that Qwest should no longer be held to its commitment. (The burden, of course, would lie with Qwest to prove the existence of the material changes and a direct connection between the changes and Qwest's commitment.) In this way, the Board could be assured that Qwest's commitment would continue for as long as it is appropriate, while Qwest could be assured that it can be released from this commitment whenever Qwest can prove the existence of material changes in circumstances.

The other concern raised by Qwest's limited commitment is that it only applies to Qwest's decision to initiate a rate proceeding. Qwest specifically reserves the right to argue in response to any rate-related filing made by any other party that imputation should end because the directory publishing business has been sold. Qwest offers no justification for this limitation and the Board can see no reason why the identity of the party initiating or participating in a future rate case should affect this issue. Again, the point is that if QCII did not sell these assets, then Qwest would never be able to make the argument that imputation is inappropriate because the assets have been sold. Only by making an unrestricted commitment that it will not assert this argument (absent a material change in circumstances) can Qwest put its customers

in nearly the same position after the sale as they currently occupy, and thereby make Board review of the proposed transaction unnecessary.

2. Qwest's other commitments

With respect to the remaining commitments identified in the Board's September 4, 2002, order, the Board finds that Qwest has made sufficient commitments on the second and third factors. (Continued investment of sufficient capital and possible future sale of Iowa properties, respectively.) Consumer Advocate argues the commitments are "exceedingly short and essentially unenforceable," but does not offer further explanation of its position. In each case, the differences between the language used in the September 4, 2002, order and in Qwest's commitments appear to be insignificant and, in any event, the Board understands Qwest to be making the commitments described in the September 4, 2002, order. Consumer Advocate's unexplained objection to these commitments is rejected.

The fourth item identified in the September 4, 2002, order concerned a showing of the effect on the financial stability of Qwest that would result from the time required for full review of the proposed transaction. Qwest's request for waiver includes information indicating it is unusually important to Qwest that the proposed transaction be closed in a timely manner. For instance, Qwest cites recent statements by a rating agency that indicate material delays in this transaction could result in another downgrade of Qwest's debt. Qwest also points out that the purchase agreement provides that either party may terminate the agreement if the

first phase of the transaction, which includes Iowa, is not closed by December 15, 2002, so an extended review could be the end of the transaction. Finally, Qwest argues that the delay inherent in a review proceeding adds risk to the transaction, risk that could imperil the transaction altogether, with "lasting adverse financial repercussions for Qwest." (Request for waiver, page 9.)

The Board finds Qwest's statements are sufficient to establish the public interest would be advanced by expedited Board action in this matter, if the other concerns are addressed as part of the process. Normally, the fact that the parties to a proposed transaction have agreed to an early termination date would be of little significance; if the Board accepted that fact as establishing a need for expedited action, then the parties to public utility reorganizations would always agree to early termination dates in order to shorten the time for Board review. However, in this case the Board is persuaded that the December 15, 2002, termination date was established, at least in part, as a result of Qwest's unusual need to close this transaction at the earliest opportunity.

CONCLUSION

In conclusion, the Board finds that Qwest has made satisfactory representations regarding its future capital investments in Iowa, its bid procedures for any future sale of Iowa properties, and the public interest detriments that could result from the time required for a full reorganization review proceeding. However, Qwest's commitment that it will not, in a future rate review proceeding, argue that imputation

is inappropriate because of the proposed transaction, is inadequate to alleviate the public interest concerns associated with the proposed transaction. The commitment is inadequate both because it is unreasonably limited in duration and because it is unreasonably limited to only Qwest-initiated proceedings to raise rates. If Qwest were to revise its first commitment to eliminate these limits, then the Board could apply the waiver standards of 199 IAC 1.3 to determine whether Board review of the proposed transaction is necessary in the public interest and, if it is not, waive the review requirements of §§ 476.76 and 476.77 and 199 IAC ch. 32.

With that final commitment, the Board could find that application of the reorganization review statute and rules would work an undue hardship on Qwest; that a waiver would not prejudice the substantial legal rights of any person; that the provisions of the rule being waived are not specifically mandated by statute or another provision of law; and that substantially equal protection of public health, safety, and welfare will be afforded by means of the various commitments. Having made those findings, the Board could then proceed to grant the requested waiver.

ORDERING CLAUSE

IT IS THEREFORE ORDERED:

The "Request For Expedited Waiver" filed by Qwest Corporation on September 19, 2002, cannot be granted in its present form. If an amended request for waiver is not filed within 14 days of the date of this order, the request will be deemed denied. The waiver will be granted if Qwest files an amended request that

renews its second, third, and fourth commitments of September 19, 2002, and includes a binding commitment that in any future rate proceeding of any nature, it will be precluded from arguing against imputation of directory publishing revenues on the grounds that the directory publishing business has been sold. Qwest may reserve any other arguments it may have against imputation. Qwest may also reserve the right to argue that it should be released from this commitment on the basis of material, changes in circumstances.

UTILITIES BOARD

/s/ Diane Munns

/s/ Mark O. Lambert

ATTEST:

/s/ Judi K. Cooper
Executive Secretary

/s/ Elliott Smith

Dated at Des Moines, Iowa, this 3rd day of October, 2002.